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   NEED/IMPORTANCE OF THE STUDY

   STATEMENT OF THE PROBLEM

   OBJECTIVES

   HYPOTHESES

   RESEARCH METHODOLOGY

   RESULTS & DISCUSSION

   FINDINGS

   RECOMMENDATIONS/SUGGESTIONS

   CONCLUSIONS

   SCOPE FOR FURTHER RESEARCH

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   REFERENCES

   APPENDIX/ANNEXURE

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- Bowersox, Donald J., Closs, David J., (1996), "Logistical Management." Tata McGraw, Hill, New Delhi.
- Hunker, H.L. and A.J. Wright (1963), "Factors of Industrial Location in Ohio" Ohio State University, Nigeria.

CONTRIBUTIONS TO BOOKS

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- Garg, Bhavet (2011): Towards a New Natural Gas Policy, Political Weekly, Viewed on January 01, 2012 http://epw.in/user/viewabstract.jsp

THE EFFICIENCY OF MARKET RISK DISCLOSURES IN JORDANIAN COMMERCIALS BANKS

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ABSTRACT

Transparency and disclosure is important ingredient of banking sector stability and this study focuses on assessing the current operational risk disclosure in Jordanian banks. So we focuses on the market risk items that Jordanian banks disclose and if comply with the central bank of Jordan requirement's. The survey methodology was adopted by testing the annual financial reports for Jordanian commercial banks. 12 banks were as a whole society. The study found evidence that, Jordanian banks primarily meet the requirement of central bank of Jordan relating to market risk disclosure, but there are many discrepancies between Jordanian banks relating to formalize the financial report to present the market risk disclosure in the same format, in additon the requirements of central bank of Jordan dose not enough when we compare it with the international bank of settlement. Our study advice to enhance current market risk disclosure practices in Jordanian banks.

KEYWORDS

Market risk, Disclosure, Basel II, Bank of International Settlement (BIS).

1.1 INTRODUCTION AND MOTIVATION TO THIS STUDY

The economy is the mainstay of any country, and became the strength of the countries which measured by the efficiency of its economy. Since the banks are the cornerstone of any economy, and the annual reports are available indicator and scale of the work of these banks, it was necessary that these reports reflect the work of those banks clearly, inclusive and transparent, which is the concept of disclosure.

The principle of information disclosure in the financial statements play an important and central in the preparation of accounting data published and this principle is considerable interest by both the Councils professional accounting or regulatory authorities on the profession, in addition to the bodies of the international exchange (Mikhail, 2006) and therefore it is for the preparation of the data that achieve adequate and proper disclosure was necessary to determine the information that should be disclosed and how disclosure by these entities (Lewis and Pendrill, 2000).

Market risk is the risk of loss from adverse movements in market prices such as commodity prices, exchange rates and interest rates [Linsmeier and Pearson (1997)]. Given the frequency and magnitude of losses arising from market risk exposures experienced by several corporate and non-corporate entities in the last decade, there has been wide-spread concern about the adequacy of market risk disclosures [see for example, AIMR (1993), AICPA (1994), and Basle Committee (1995)].

Commercial banks have been disclosing maturity gap data (a type of quantitative market risk disclosure) for some time. Ryan (1997) refers to these disclosures as the best extant example of ex ante risk disclosures. Banks also provide some qualitative information on their interest rate risk in their annual reports. We investigate the efficacy of maturity gap and interest rate risk management policy disclosures by commercial banks in indicating banks' interest rate risk. Barth (1998) argues that "although these disclosures are not available for most firms, they are suggestive about disclosures that would be useful to investors of nonregulated firms" [quoted in Schrand and Elliott (1998)]. Thus, our study provides preliminary evidence on the efficacy of market risk disclosures mandated by SEC (1997).

In addition to the above, there is growing interest by the Bank of International Settlements and practices to expand the concept of disclosure of market risk to enhance the transparency and clarity in the work of the banking sector and its activities are beyond those existing in the legislation of accounting and local legislation and of the Central Bank and Securities Commission in each state (Institute of International Finance, 2003).

And here we know that a disclosure about market risk is necessary as part inherent in the nature of banking activity basis, hence the need arises to disclose the nature of this important part in the annual financial reports of banks through disclosed and the nature and characteristics.

1.2 THE PROBLEM OF THE STUDY

In their annual reports, banking institutions provide stakeholders with relevant financial, operational and strategic information. As a major task of banks is to measure and manage the
risks that arise from their business activities and as stakeholders are generally concerned with
the levels of risks that a financial institution has taken to achieve a particular outcome, the reporting and discussion of these risks are an integral part in banks' annual reports.

Under Pillar 3 financial institutions are required to provide detailed information on their capital structure and adequacy, as well as information on the size and assessment of risk exposures. The aim is to provide stakeholders and market participant with an opportunity to better being able to assess the riskiness of the institution.

In this paper we examine the quantity and quality of market risk measurement and management information that is currently provided by jordanian commercial banks annual reports and assess the results in light of the disclosure requirements for market risks as put forward by the BCBS(Basel Committee on Banking Supervision).

1.3THE IMPORTANCE OF THE STUDY

The importance of the study are to detect the concept and the adequacy of the market risk disclosure and the nature of the contiguity of the banking activity and imposed by this nature. And through the preparation of financial statements contain a high level of disclosure to market risk in order to enhance the transparency of banks and to strengthen the market system by encouraging banks to provide the public (public) and participants in the market (market participant) the information they need in order to assess the financial position of banks and the performance and activities and exposure to economic risk. The importance of this issue because of the weak practices in market risk management, which was the part from many reasons for the failure of banks and banking crises in the world (BIS, 1999).

1.4 PURPOSE OF THE STUDY

The purpose of this study is to measure the current level of disclosure for the Jordanian banks in market risk, through the examination of annual financial reports for Jordanian commercial banks and if the current practices comply with BIS and international practices.

2 – LITERATURE REVIEW

2.1 MARKET RISKS: FRAMEWORK FOR DEFINITIONS AND DIMENSIONS

Market risk is the risk of loss from adverse movements in market prices such as commodity prices, exchange rates and interest rates [Linsmeier and Pearson (1997)]. Given the frequency and magnitude of losses arising from market risk exposures experienced by several corporate and non-corporate entities in the last decade, there has been wide-spread concern about the adequacy of market risk disclosures [see for example, AIMR (1993), AICPA (1994), and Basle Committee (1995)].

In response to these concerns the Securities & Exchange Commission (SEC) and the Financial Accounting Standards Board (FASB) have issued new disclosure requirements pertaining to market risk. SEC (1997) mandates disclosure of quantitative as well as qualitative information about market risk exposure of registrants. The accounting standard on derivatives and hedging, SFAS 133, significantly changes the accounting for derivatives and requires disclosure of information on market risk exposures.

However, there is disagreement over the desirability or usefulness of market risk disclosures. For example, critics argue that investors may find the SEC (1997) disclosures misleading and uninformative [Culp and Miller (1996), Lehn (1997), Loman and Montgomery (1997)]. There is little extant evidence on the efficacy of quantitative market risk disclosures and no prior evidence on the efficacy of qualitative market risk disclosures primarily because firms generally don't voluntarily provide sufficiently detailed quantitative or qualitative market risk disclosures [see Schrand and Elliott (1998), Rajgopal (1998) and Rajgopal and Venkatachalam (1998) and Wong (1998)].

Commercial banks have been disclosing maturity gap data (a type of quantitative market risk disclosure) for some time. Ryan (1997) refers to these disclosures as the best extant example of ex ante risk disclosures. Banks also provide some qualitative information on their interest rate risk in their annual reports. We investigate the efficacy of maturity gap and interest rate risk management policy disclosures by commercial banks in indicating banks' interest rate risk. Barth (1998) argues that "although these disclosures are not available for most firms, they are suggestive about disclosures that would be useful to investors of nonregulated firms" [quoted in Schrand and Elliott (1998)]. Thus, our study provides preliminary evidence on the efficacy of market risk disclosures mandated by SEC (1997).

We focus on gap data because despite its prevalence, there is disagreement among banks about its usefulness. For example, a recent survey of risk management practices in the banking industry suggests a reduction in the use of gap disclosures because of their alleged limitations [McGuire (1998)]. On the other hand, gap data potentially help quantify the effect of interest rate changes on net interest income [Toevs (1983)].

Furthermore, they are relatively more objective than earnings sensitivity or value-at-risk estimates that require relatively extensive subjective assumptions. Thus, a priori, it is not clear that gap data are not informative about market risks.

With respect to qualitative disclosures we focus on studying risk management policy statements of banks because relative to other qualitative disclosures they are likely to be easier to interpret. If outsiders cannot meaningfully interpret policy statements, it is unlikely that they will be able to meaningfully interpret other qualitative disclosures such as the "context of an entity's overall risk management profile" required by SFAS 133.

2.2 FRAMEWORK FOR DISCLOSURE OF MARKET RISK IN BASEL II

2.2.1 Market risk in the trading book

The framework for disclosure of market risk in this section is given by the solvency requirements published in 1996 by the Committee in the "Amendment to the Capital Accord to incorporate market risks" (the Amendment hereafter).18 This framework ensures a minimum degree of transparency and consistency of concepts used in the disclosures. The Amendment describes a standardized method and an internal models approach (IMA). The market risks covered are interest rate risk and equity risk in the trading portfolios and currency risk and commodity risk for the whole bank.

A-standardized approach, the Committee proposes to use the capital charge as the risk indicator, to allow comparison between different categories of risk and between institutions. Banks with approval from their supervisor to use internal market risk models for the calculation of the solvency requirement will also use these models to disclose the level and characteristics of market risk. The internal models are based on the value-at-risk concept, which will be used as the basis of disclosure. Appendix 4 provides greater detail on market risk disclosures, along with suggested templates.

A.1 The main qualitative core disclosure is the specification of the portfolios covered by the standardized approach and which of the available measurement methodologies within the standardized approach is chosen by the bank. For instance, whether the bank has applied the maturity or the duration method for the measurement of interest rate risk in the trading book.

A.2 The quantitative core disclosure gives information about the capital requirements for interest rate risk, equity position risk, foreign exchange risk and commodity risk. In addition, the capital charge for option positions is disclosed.

A.3 Supplementary quantitative disclosures give the capital charges specified for different risk categories and portfolios. For interest rate risk in the trading book the risk categories are the distinction between general and specific market risk and the different points on the yield curve. The different components of the capital charge for interest rate risk make use of these distinctions and disclosure of these components can be useful supplementary information. For equity positions the standardised approach gives risk weights for general and specific market risk and makes a further distinction between index and arbitrage positions. Supplementary quantitative disclosure of equity positions can give additional information using these concepts and definitions. In a similar way, positions in foreign exchange and commodities can be disaggregated.

A.4 An additional risk concept is the daily variability of profits and losses on the trading positions concerned. Especially for positions for which the standardised approach is not a very precise risk indicator, disclosure of the daily variability of profits and losses gives important additional information.

The movement of portfolios between the standardized approach and the IMA may also be disclosed.

B- Internal Models Approach (IMA)

The Amendment introduced the possibility for banks, after supervisory approval, to use their internal models for the assessment of the capital requirements for market risk as an alternative for the standardised approach. Since the IMA offers a consistent framework for value-at-risk calculation, the risk profiles of banks using IMA are, to a large extent, comparable, although banks have some discretion with respect to certain characteristics (e.g. the observation period).

B.1 The core qualitative disclosures give information about the coverage of the IMA, the characteristics of the models used and the stress test program. Banks disclose the (partial) acceptance given by the supervisor.

B.2 The core quantitative disclosures concern value-at-risk data and the back test results on an aggregated level. The value-at-risk measure provides a first indication of the level of market risk. The IMA uses back test results as an indication of the performance of bank's model during the review period. The supervisor may increase the multiplication factor, and thus the capital requirement, if the number of "outliers" or breaches is greater than four, and the model can be rejected if the number of outliers is greater than nine. The back test may use hypothetical or real data19. Both back tests are described in the Market Risk Amendment. The core disclosure is the result for the total IMA portfolio.

B.3 The purpose of the supplementary disclosures is to provide the market with more details about the coverage of the IMA, the characteristics of the risk models used, the most important aspects of the risk profiles and the components of back test results.

2.3 MARKET RISK IN ACCOUNTING STANDARDS

Accounting standards setters encourage incentives for improved risk management and its disclosure. Both International Accounting Standards (IAS)3 and the Statements of Financial Accounting Standards (FASB Statements) contain extensive standards on the treatment of credit risk (IAS 30; FASB Statements 5, 15, 114, and 118), while disclosure on market risk is not explicitly regulated today. The increasing awareness of the relevance of other risks beside credit risk is reflected in IAS 30 paragraphs 50 to 52, dealing with general banking risks under which market risk can be assumed. These rules demand banks to report the amount set aside for future losses and other unforeseeable contingencies due to general banking risks as well as to abstain from including credits or reductions in such amounts in the net profit or/loss.

Also IFRS 7 indicates to put disclosures about market risk in the annual reports , which includes:

- a sensitivity analysis of each type of market risk to which the entity is exposed

- additional information if the sensitivity analysis is not representative of the entity's risk exposure (for example because exposures during the year were different to exposures at year-end).
- IFRS 7 provides that if an entity prepares a sensitivity analysis such as value-at-risk for management purposes that reflects interdependencies of more than one component of market risk (for instance, interest risk and foreign currency risk combined), it may disclose that analysis instead of a separate sensitivity analysis for each type of market risk

2.4 WHY WE ASSESS BANK DISCLOSURE PRACTICES

Enhanced accounting disclosure leads to better transparency and stronger market discipline in the banking sector. The third pillar of Basel II, Basel Core Principles No.21, and recently the Policy Brief released by the OECD "Corporate Governance of Banks" Task Force, have explicitly asked for better disclosures by banks to allow the market to have a better picture of the overall risk position of the banks and to allow the counterparties of the banks to price and deal appropriately. More disclosures should reduce information asymmetry between those with privileged information and outside small investors, and facilitate more efficient monitoring, because sufficient information is necessary for market participants to exert effective disciplinary roles. 1 According to a McKinsey "Global Investor and Emerging Market Policymaker Opinion Survey on Corporate Governance", "accounting disclosure" was listed as the number one most important factor considered by 71% of investors surveyed, and "enhanced disclosure" was named as number one key progress area by 44% of policymakers.

Accounting disclosure is raised to a particularly high level of importance for banking organizations compared to non-financial firms, for banks are inherently more opaque. Accounting reports are almost the sole source of information for bank investors and other stakeholders. Banks own few physical and visible assets, and investors can acquire a sense of a bank's performance and asset quality only from accounting numbers. Earnings numbers alone are not adequate for assessing the valuation of banks, the main business of which is to take risks and to provide liquidity (and thus earnings can be inflated through doing more of them). Thus profitability does not give investors the whole picture of the bank's financial situation, until risk profile of the bank is holistically disclosed. Finally, aggregate accounting numbers (e.g., total profits, total loans) without reasonable level of breakdown is less informative for banks than it is for industrial firms, because the most important information usually lies in the details of the sources of income and expenses, or quality of assets. Investors need this information to make judgments on which incomes are sustainable and which expenses are recurring.

Finally, in our study we examine the marke risk disclosure practices for Jordanian banks. We gather information from the 2010 annual reports of these institutions. We adopt a content-analysis approach, as information in risk management reports is predominantly of qualitative nature. The focus of our study is the disclosure of information on market risk measurement and management practices and methodologies in light of approaching implementation of the Basel II framework.

3 – RESEARCH DESIGN

In this chapter we will present the design of our research. First, the research factors which indicate for market risk sufficiency will be discussed. Second, the sample selection and composition is presented. Then, the empirical model we use to test our factors will be explained and analysis:

3.1 RESEARCH FACTORS

Based on reviewing many literatures, Jordanian regulation, Basel II and best practices, we decided to measure the operational risk disclosure by defining the following three variables , Hierarchical issues, Regulatory Issues and Definition issues.

3.2 SAMPLE SELECTION

In our sample we include all Jordanian commerical banks, so the study population includes all Jordanian banks up to the year (2010)'s which is (12) Jordanian commerical banks. The study sample included all of these banks,'s that represent sampling units.

4. DATA ANALYSES AND RESULTS

The following tables shows the disclosure items for all Jordanian banks and if comply with our research factors by match each factor with annual report for each bank.

TABLE -1

Disclosure Item	Assets & Liability managment committee (ALCO)	Analyze cash flow exposures	Analyze Market Risk Exposures	Definition of Market Risk	The Govrner of Market risk	Tools used for measuring & managing market risk	Details notes for market risk sensitivity analysis	Market risk impact on the income & owner equity
Arab Bank Group	√	√	√	√	√	×	×	×
Housing Bank for Trade and Finance	√	×	√	×	×	×	×	×
Ahli Jordan Bank	√	×	√	×	×	×	×	×
Cairo Amman Bank	√	√	√	√	√	×	×	√
Union Bank	√	×	×	×	√	×	×	×
Jordan Kuwait Bank	√	×	√	√	×	×	×	√
Bank Of Jordan	√	√	√	√	√	×	×	√
Jordan Islamic bank	√	√	√	×	√	×	×	×
Capital Bank	√	√	√	√	√	×	×	√
Arab Jordan Investment Bank (AJIB).	×	×	×	×	×	×	×	×
Islamic international Arab bank	√	√	√	√	√	×	×	√
Societe Generale de Banque / Jordanie	√	×	√	×	√	×	×	×

TABLE - 2

Disclosure Item	Mathmatical Clarification for Basis piont value method in measuring market risk	Mathmatical Clarification for Value at risk-VAR- method in measuring market risk	Stress Testeing – aims and calculation techniqes	exposures to fluctuations in variables such as interest rates, foreign exchange, and commodity prices	The effect of market risk in the trading book and banking book.
Arab Bank Group	×	×	√	√	√
Housing Bank for Trade and Finance	×	×	√	×	×
Ahli Jordan Bank	×	×	×	×	×
Cairo Amman Bank	√	√	×	×	√
Union Bank	√	×	√	×	×
Jordan Kuwait Bank	√	√	×	×	×
Bank Of Jordan	√	√	×	×	√
Jordan Islamic bank	×	×	×	×	×
Capital Bank	√	×	×	×	×
Arab Jordan Investment Bank (AJIB).	×	×	×	×	×
Islamic international Arab bank	√	×	×	×	×
Societe Generale de Banque / Jordanie	×	×	×	×	×

TABLE -3- SUMMARY

Disclosure item	% percentage
Assets & Liability managment committee (ALCO)	92%
Analyze cash flow exposures	50%
Analyze Market Risk Exposures	83%
Definition of Market Risk	50%
The Govrner of Market risk	67%
Tools used for measuring & managing market risk	70%
Details notes for market risk sensitivity analysis	0%
Market risk impact on the income & owner equity	42%
Mathmatical Clarification for Basis piont value method in measuring market risk	50%
Mathmatical Clarification for Value at risk-VAR- method in measuring market risk	25%
Stress Testeing –aims and calculation techniqes	40%
Exposures to fluctuations in variables such as interest rates, foreign exchange, and commodity prices	8%
The effect of market risk in the trading book and banking book.	25%

% percentage: equal the existence of item in banks divided on total number of banks

From the above table we found evidence that Jordanian banks have overall market risk disclosures, especially in disclosing risk management framework , establishing Assets & Liability managment committee (ALCO), Analyze Market Risk Exposures and Analyze Market Risk Exposures . While we mention that there is a negative attitude for giving details about Market risk impact on the income & owner equity, Stress Testeing –aims and calculation techniqes, and Exposures to fluctuations in variables such as interest
rates, foreign exchange, and commodity prices

5- RESULTS

The previous sections of this chapter presented the results of our research. In this section, we will recap and analyze these results.

First, by analyzing Jordanian banks annual reports, we provide evidence that both extent and content of banks' disclosure on market risk are substantially good, reflecting the intensified risk management efforts of banks, supervisors, and other agents.

Second, we found evidence that, Jordanian banks primarily meet the requirement of central bank of Jordan relating to market risk disclosure and in some times enhance and exceed above the requirement.

Third, there are many discrepancies between Jordanian banks relating to formalize the financial report to present the market risk disclosure in the same format, in another word we found many difficulties to track where Jordanian banks disclose on market risk and in at what pages.

Fourth, the requirements of central bank of Jordan dose not enough when we compare it with the international bank of settlement.

Finally, under international accounting standards the disclosure on market risk is not explicitly regulated-insufficient- until today and the standards focused on credit risk.

6 – RECOMMENDATIONS

First, we advise central bank of Jordan to enhance the market risk disclosure requirements by impose on Jordanian banks to give more details on managing market risk.

Second, central bank of Jordan should require banks to have an effective system in place to identify measure, monitor and control market risks as part of an overall approach to risk management.

Finally, a higher level of disclosure would allow for an evaluation using a more detailed index especially quantitative disclosures related to market risk could provide a fruitful basis for future research.

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